111 (3) No. 08-138

Supreme Court, U.S.
FILED
NOV 7 - 2008
OFFICE OF THE CLERK

In The Supreme Court of the United States

MOLA DEVELOPMENT CORPORATION,

Petitioner,

v.

UNITED STATES,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

REPLY TO BRIEF IN OPPOSITION

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PETITIONER'S REPLY MEMORANDUM

The government tries to minimize the importance of this case by casting the dispute as an issue of fact and claiming that any lower court error is of no import because there are only 15 remaining *Winstar* cases. Mola disagrees with these characterizations. Recent events make it abundantly clear that the issues which Mola and other *Winstar* plaintiffs face are still relevant today—even more so than they were only three months ago. One only has to look in a local newspaper on any given day to see that history is repeating itself. Private enterprises are once again bailing out the government insurance fund through the acquisition of failing financial institutions. While the rules of the game may have changed since the 1980s, the government's ability to contract with the acquiring institutions and the institutions' ability to hold the government to the terms of those contracts are very much at issue today. Will today's rescuing institutions suffer the same fate as Mola and the majority of the other *Winstar* plaintiffs?

The Federal Circuit and Court of Federal Claims ruled on the facts of this case in a manner targeted to create rules and standards that depart from this Court's ruling in *United States v. Winstar*, 518 U.S. 839 (1996), and that are inconsistent with other Federal Circuit precedent such as *Fifth Third Bank of Western Ohio v. United States*, 402 F.2d 1221 (Fed. Cir. 2005). These courts cited law from *Winstar*, *Fifth Third Bank* and *Anderson v. United States*, 244 F.3d 1343, 1353 (Fed. Cir. 2003), but they did not adhere to the precedent established by

those cases. Specifically, the Federal Circuit "found" that "Mola points to no evidence of any negotiations about the regulatory treatment of goodwill that could serve as evidence that the government agreed to a goodwill contract." In explaining this conclusion, the Federal Circuit relied on *D & N Bank v. United States*, 331 F.3d 1374, 1378 (Fed. Cir. 2003), for the propositions that regulatory proclamations and an agency's performance of its regulatory or sovereign functions are insufficient to create contractual obligations absent a single integrated document. *D & N Bank,* however, is inapposite because that case truly involved nothing more than a stamp of approval by the regulatory authority. *D & N Bank* did not involve the bargained for exchange regarding the supervisory designation that was present in Mola's case. In extending *D & N Bank* to Mola's situation, the Federal Circuit created a standard whereby nothing that could be construed as a regulatory function could also be construed as a contractual commitment. That standard clearly contravenes the Federal Circuit's prior ruling that the FHLBB could memorialize its contractual commitments in agency documents. *Fifth Third Bank*, 402 F.2d at 1234. Significantly, the FHLBB had no other way of doing business. It also contravenes this Court's instruction in *Winstar*, which described the requisites of a contractual agreement for the regulatory treatment of goodwill:

> [T]he [FHLBB] resolutions, Forbearance Letters, and other documents setting forth the accounting treatment to be accorded supervisory

> goodwill generated by the transactions were not mere statements of then-current regulatory policy, but in each instance were terms in an allocation of risk of regulatory change that was essential to the contract between the parties.

Winstar, 518 U.S. at 909. *Winstar* did not mandate any magic language or the use of a single integrated contract to establish the existence of a *Winstar* contract, and the Federal Circuit and Court of Federal Claims should not be allowed to write such requirements into the body of law governing claims against the government.

In Mola's case, the Federal Circuit also set up a standard by which any agreement for the use of supervisory goodwill that was consistent with Memorandum SP-24 and GAAP, and did not require an extended amortization period beyond that permitted by GAAP, was insufficient to create a contractual commitment. The Federal Circuit drew that same line in *First Federal Lincoln Bank v. United States*, 518 F.3d 1208 (Fed. Cir. 2008). *Winstar* did not set this limitation which is without logic or basis. Decisions upholding the existence of *Winstar* contracts are often based on the fact that the government gave an institution something more than what was allowed by existing regulations, such as extended amortization periods. While an extended amortization period can be one sign of a *Winstar* contract, it is not a prerequisite to a *Winstar* contract. One of the *Winstar* test cases involved an amortization period of not more than 25 years.

Winstar, 518 U.S. at 867. It is clear that there must have been a contract in cases where the parties' agreement exceeded the government's regulatory authority, because it would be the only basis for supporting the agreement, but the Federal Circuit's conclusion that there can be no contract without an extended amortization period does not logically follow from that principle.

Acquiring financial institutions deliberately contracted for the regulatory treatment of goodwill because they knew that regulations could change, and they needed protection from that change. A financial institution's need for a promise regarding the regulatory treatment of goodwill did not differ depending on whether the amortization period was 25 or 40 years. The bargained for treatment of supervisory goodwill should be the same regardless of whether the number of years needed for amortization were consistent with GAAP. Any other interpretation defies this Court's concept that it would have been "madness" for an acquiring institution not to get an upfront promise from the government. *Winstar*, 518 U.S. at 863. While a party cannot rest only on the rationality or the irrationality of a merger, the "madness" concept does reinforce the notion that a contract for the use of supervisory goodwill could be consistent with the government's regulatory authority.

The Federal Circuit and Court of Federal Claims' substantial departures from this Court's previous ruling in *Winstar* and the Federal Circuit's ruling in *Fifth Third Bank* are confirmed by Judge

Newman's dissent in the case below. In her dissenting opinion, she wrote:

> The contract between Mola and the federal government was an integrated combination of various documents involving the government, Mola and its subsidiary Charter, and the insolvent Merit Savings Association. Mola agreed to contribute approximately $2.5 million in cash to the merged Charter/Merit thrift institution, plus an additional $1 million to Merit's shareholders, and the government agreed to classify the merger as 'supervisory'.

App. 24a.

Judge Newman went on to identify the numerous documents that confirm the parties' contract including Mola's H-(e)3 application, the Consolidated Charter & Merit Balance Sheet, FHLBSF memoranda, FHLBSF correspondence, and the FHLBB certificate deeming Merit a supervisory case. App. 25a-27a. All of these documents pertain to Mola's quid pro quo bargain for the supervisory designation. The supervisory designation achieved the regulatory treatment of goodwill which Mola sought. Judge Newman also explained that the parties had engaged in multiple rounds of negotiation and that supervisory goodwill was an essential component of those negotiations. Under *Winstar*, FHLBB resolutions, forbearance letters and other regulatory documents setting forth the

regulatory treatment of goodwill were enough to support the existence of a contract for supervisory goodwill. *Winstar*, 518 U.S. at 909. Further, in some cases, evidence of the contract could come from discussions and surrounding circumstances. *Fifth Third Bank*, 402 F.3d at 1235. Mola's case is no different.

Based on Judge Newman's findings, it is clear that there was at least *some evidence* of a contract for supervisory goodwill between the parties. The majority panel could have only determined that there was *no evidence* by implying standards and criteria for contract formation in *Winstar* cases that were not previously there. In this instance, those standards were a prohibition against contracts that were consistent with the then existing regulatory framework and a need for a single, integrated document or "magic language" that explicitly spelled out the terms of the contract. Had Mola used the words "supervisory goodwill" instead of "supervisory merger", the Federal Circuit may have come to a different conclusion. The semantic distinction is unwarranted when Mola needed the supervisory designation in order to use supervisory goodwill for the purpose of meeting regulatory capital requirements.

Finally, contrary to the government's assertion, Mola does not argue that every merger that the government approved in the early 1980s resulted in a contract with the government. Where there is no quid pro quo or bargained for exchange with the government, there is no contract. *See e.g.*, *D & N Bank*, 331 F.3d at 1378. The supervisory

designation in and of itself is insufficient to establish the existence of a contract for supervisory goodwill. But, where a party bargains for that designation in a context where the acquiring institution needs to count supervisory goodwill towards its capital requirement, and the parties come to an agreement consistent with ordinary principles of contract law, it cannot be said that there is no contract for supervisory goodwill as a matter of law.

The Federal Circuit changed the landscape in which *Winstar* cases are decided through its rulings on the issues in the case below. It is not enough that the Federal Circuit cited the right law if it applied the facts of the case in a manner designed to defeat that law. Given the repeat-game nature of the *Winstar* cases, and the lower courts' increasing departures from the *Winstar* mold, it is important that the Court hear this case. Otherwise, the Federal Circuit can make new law and depart from the standards this Court set forth in *Winstar*, without any check or balance, simply because the government declares the decision to be an issue of fact.

Respectfully Submitted,

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November 7, 2008